



# Government Property Lease Excise Tax (GPLET)

Kevin McCarthy



## GPLET Definition

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- Mechanism to tax private concerns on certain government properties
- Officially an “excise” tax that is based on the square footage & use of a building rather than property value
- Enacted in 1996 to replace tax on possessory interests that was repealed in 1995
- GPLET is levied on property that is owned by a city, town, county or county stadium district and leased to a private concern



# GPLET - How did we get here?

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- Early 80's, cities began to aggressively use their tax exempt status to shield private development from property tax
- Legislature enacted a possessory interest tax in 1985 - a property tax on privately held improvements on government-owned property
- Newly created tax provided exemptions to existing deals created prior to April 1, 1985
- In 1993, Court struck down exemptions as unconstitutional in the Scottsdale Princess case



## GPLET Enacted in 1996

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- The Legislature stated the purpose was to:
  - Be an excise tax, and not an *ad valorem* tax
  - Address the problems that existed with the possessory interest tax (i.e. exemptions)
  - **Make whole the taxing jurisdictions that depended on revenues under the prior law**



## GPLET 1996 Structure

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- Applied to cities, counties and county stadium districts
- Based on square footage & type of building - not its value
- Exemptions found unconstitutional under the possessory interest tax included as exemptions under GPLET
- GPLET collections distributed to taxing jurisdictions as follows:
  - Schools 73%, Counties 13%, Comm Colleges 7%, Cities 7%
- Maintained 8-year tax abatement in central business district



## GPLET 1996 Structure

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- GPLET rates lower compared to possessory interest tax
- Rates reduced 20% every 10 years until reaching zero in the 50<sup>th</sup> year
- By late 90's, dramatic expansion of GPLET got attention of policymakers
- Citizens Finance Review Commission recommends significant reforms:
  - Expand to all government jurisdictions
  - After abatement property should pay tax commensurate with the property tax in the area



## 2010 GPLET Reforms

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- Maximum lease 25 years, including 8-year abatement
- Rates nearly doubled but still lower than property taxes
- Rates adjusted annually by new construction inflation index
- CBD defined-single & contiguous geographical area within slum/blight, no larger than  $\geq$  of 5% of total land area or 640 acres
- City required to notify all taxing entities 60 days prior to approval, provide economic fiscal benefit analysis 30 days prior
- GPLET lease filed with County Recorder, Treasurer, and DOR



# AG 2015 Audit Revealed Problems

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- 2010 revisions have not resulted in increased revenue as expected
  - Nearly half of 268 leases are under 8-yr abatement
- 45% paying GPLET under old rate structure/only 6% pay new rates
- Many cases in which GPLET incorrectly calculated
- GPLET distributions to jurisdictions done incorrectly
- Only 3 of 7 counties with GPLET reported GPLET values to ADE
- County Treasurers failed to assess penalties and interest on delinquent GPLET payments-loss of revenue to counties
- Overall, governmental entities indicated a general lack of understanding of GPLET requirements
- Success of tax abatement in promoting redevelopment unknown





## 2017 GPLET Reform; HB2213

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- Limited any GPLET with abatement to 8 years in total
  - Eliminated the “tail” or years 9-25
  - Avoids complication of mixing GPLET revenue to tax system
- Lessor (government) now in charge of calculating tax
  - Designed to improve compliance, accuracy
- Gov lessor required to post lease agreements to official website, provide information to DOR
- Requires DOR to review any further grandfathering of pre-2010 rates



# Englehorn v Phoenix

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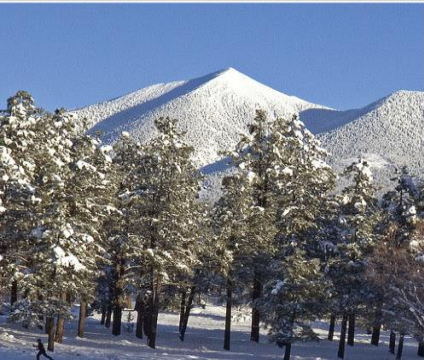
- Goldwater lawsuit contesting GPLET for *Derby Roosevelt Row* apartments
- \$36M, 19-story multiuse tower: 211 micro apts + 4,500 sqft of retail space + parking
- 8 year abatement, 25 year total GPLET deal
- Count 1: Gift Clause (Art IX, §7)
  - Abatement is valued at \$4 million; 25 year deal is valued at \$8.4M in reduced taxes
  - Taxpayer support does not constitute a public purpose, profits go to private entity/investors
  - Many apartments have been built in the area without a tax subsidy
- Count 2: Uniformity (Art IX, §1)
  - Gov't is to tax equally within same class of property; deal interrupts this demand
  - Non-uniform tax rates among identically-used property in the same industry in the same city
  - GPLET abatement allowance only in a “central business district” also runs afoul



## Englehorn v Phoenix (cont)

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- Count 3: Special Law Clause (Art IV, pt. 2, §19)
  - “No local or special laws shall be enacted in... (9) assessment and collection of taxes.. (13) Or granting to any corporation, association or individual special or exclusive privileges... (20) when a general law is applicable”
  - Classification consisting of 1 developer does not encompass all members of the relevant class
- Count 4: Conveyance to Evade Taxation (Art IX, §2 (12))
  - “No property shall be exempt which has been conveyed to evade taxation.”
- Count 5: Mandatory Competitive Bidding (A.R.S. § 9-402)
  - Leased land/improvement to prime lessee not competitively bid; not in compliance with § 9-402
- Count 6: Arbitrary and Capricious Blight Designation (A.R.S. § 42-6209, § 36-1471)
  - City relies on 1979 declaration of slum/blight that is no longer applicable to the area



# City of Flagstaff Perspective

General Session - Panel Discussion on Government Property Lease Excise Tax

Arizona Tax Conference  
September 1, 2017



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# Welcome to Flagstaff!

Population: 70,000  
Including NAU (30,000)

Elevation: 7,000

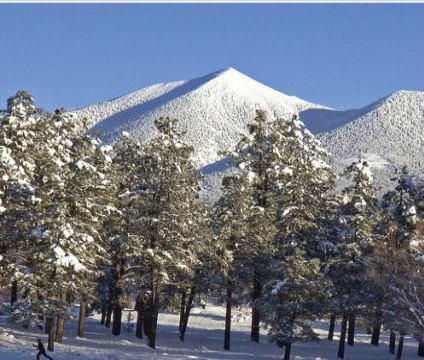
Economic Drivers: NAU, Tourism,  
Government

Niche Industries: Astronomy, Bio-Medical,  
Manufacturing



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# Regional Influences

- Colorado Plateau
- Grand Canyon gateway
- Transportation crossroads  
(I-17, 89A, Route 66, I-40, Railroad)
- Navajo, Hopi, other cultures
- Tourism



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# City Economic Challenges & Programs

## Challenges:

- High cost of workforce housing
- Small workforce
- Expensive land
- Tourism/service jobs generally low wage

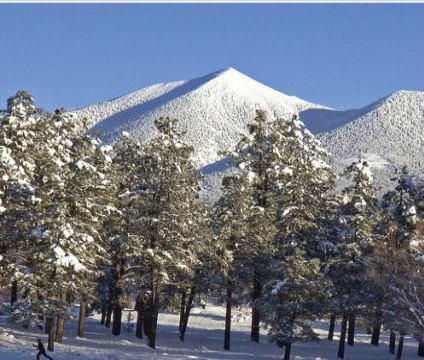
## City Programs:

- Business attraction
- Business retention and expansion



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# City as Property Owner

- City owns property for government operations and community needs.
- Community wants to preserve land. Flagstaff has acquired and designated almost 3,300 acres as open space per voter approval.



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# City Property is Special

- City property is exempt from property tax. (Arizona Constitution)  
~ Coconino County avg. property tax  
\$9.54/\$100 of assessed valuation/year
- City buildings when leased are subject to a government property lease excise tax (GPLET), except for 15 exemptions. A.R.S. § 42-6201 et seq. Lessee pays.  
~ \$0.86 – 3.49/sq.ft./year (B rates)
- City has power of eminent domain; voters have power of initiative; State has powers (such as setting GPLET rates, preemption).



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# How may the City use its property to promote economic development or serve community needs?



**1: Lease City Land (no property tax on land)**  
~ What land?

**2: Lease City Building (no property tax; pay GPLET tax or exempt)**  
~ What empty buildings?



**3. City pays for new City Building, then Leases (ditto)**  
~ Cost, financing?

**4. Property Tax Abatement Agreement (City Takes Title to Developer's Land and Building, Leases Back to Developer) (ditto)**

~ Public use and direct community benefit?

~ Developer does not need to qualify for one of 15 exemptions to be exempt from GPLET, if using A.R.S. § 42-6209 (central business district/redevelopment exception to GPLET)



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# How is the City using its property to promote economic development or serve community needs?

## Overview of City Building Leases

1. Property tax abatement agreements (3)
2. City building leases - GPLET exempt (many)
3. City building leases – GPLET applies (few)



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# Property Tax Abatement Agreements (only 3 – all pre-2010)

## Flagstaff perspective –

- City takes conservative approach
- Citizens and local paper are very engaged
- Used only for business retention or expansion
- Have exceeded performance measures



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# Joy Cone



Employs 130 in Flagstaff  
Manufactures ice cream cones



2001 Phase 1 constructed (180K sq. feet)

2009 Development Agreement (2009-2023)

- Arizona Commerce Authority initiative
- Transfer property to City/leaseback to Joy
- Joy to construct 65K sq. ft., supply jobs and insurance, misc.
- Estimated total \$3 million property tax savings/loss (net GPLET)

2012 New batter room (\$1 million project)

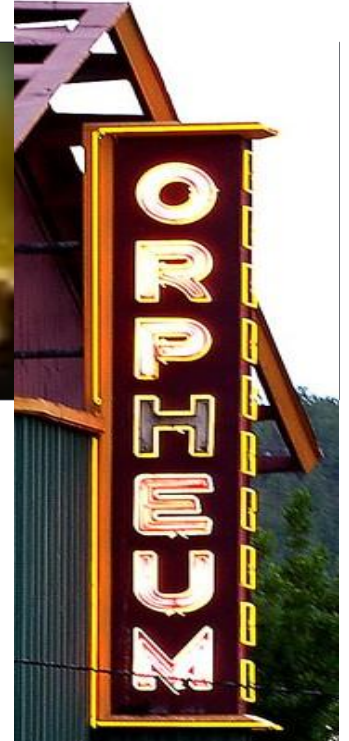


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# Orpheum Theater



Public performing arts venue, downtown anchor  
Since 1917 (Happy 100 year Anniversary!)

2009 Development Agreement (2009-2017)

- Transfer property to City/leaseback to Orpheum
- Orpheum to operate for musical, theatrical, cultural events
- Orpheum to construct tenant improvements (specified)
- Estimated property tax savings/loss of \$96,400

Exempt from GPLET, A.R.S. § 42-6208(4) (entertainment).



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# Nestle Purina PetCare (chap.1)



Employs 310  
Manufactures pet food

## 2003 Development Agreement

- Transfer property to City/leaseback to Purina
- Purina to construct 100K sq.ft. expansion, more jobs for community
- Total tax savings/loss of \$480K (amended before reaching \$1.1 million limit)

## 2008 Amendment (2008- 2016)

- Transferred additional property to City/leaseback to Purina
- Purina to construct 94K sq.ft. warehouse, plus parking, commitment to about 50 more jobs
- Purina to convey land for public street, sell land for Fire Station to City
- Estimated property tax savings/loss of \$3.5 million (net GPLET)

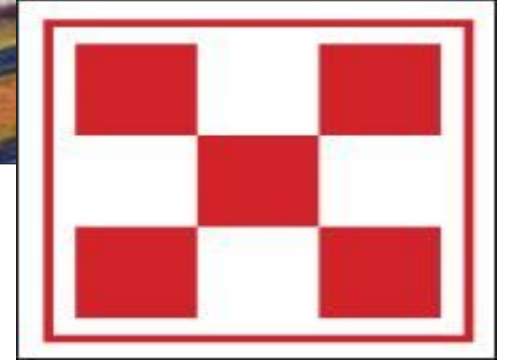


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# Nestle Purina PetCare (chap.2)



## PRODUCTION DOUBLES!

2016 Amendment (2016-2017)

- NP to mitigate odor, operate odor reduction equipment for at least 10 years
- NP to dedicate Urban Trail connection
- Estimated property tax savings/loss of \$800K (but still under \$3.5 million total)



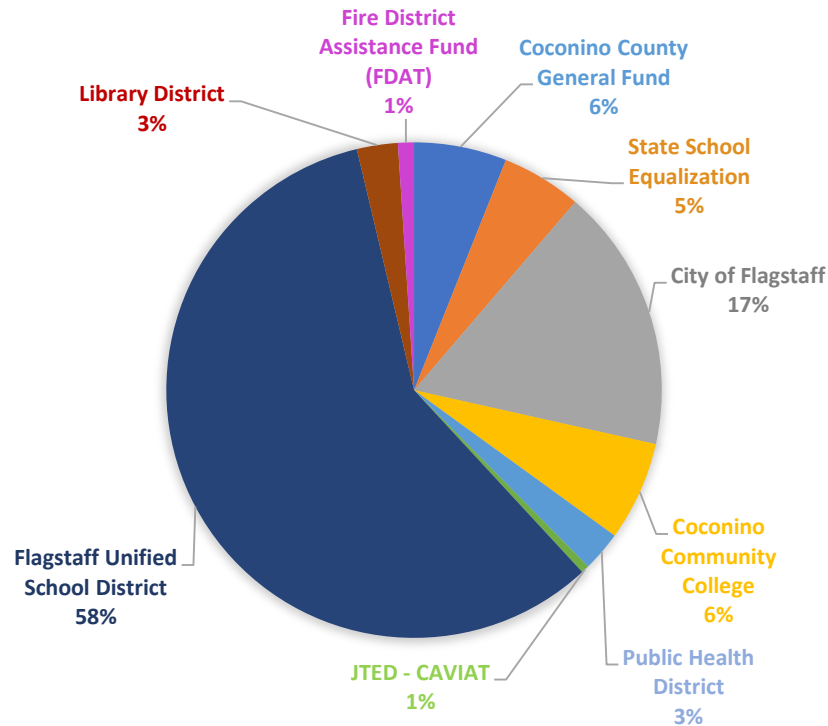
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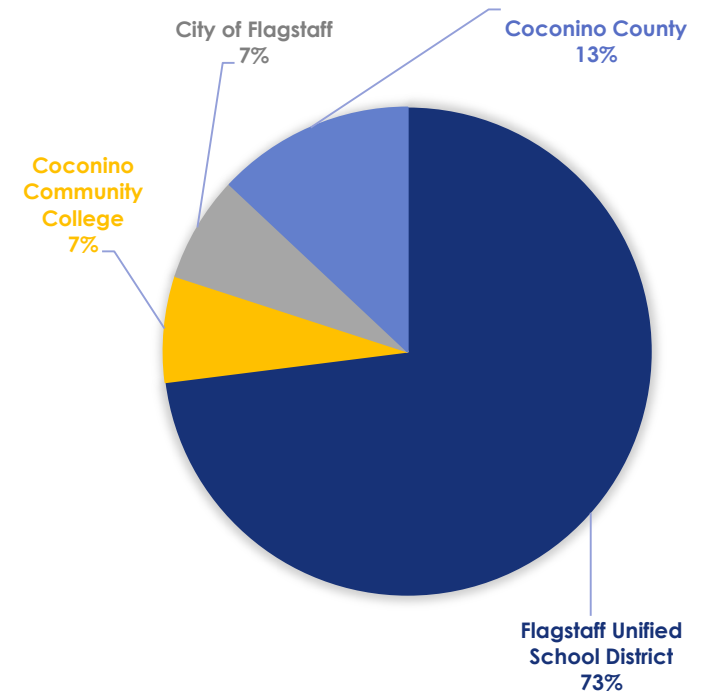


# Property tax vs. GPLET – where does the money go?

Property tax

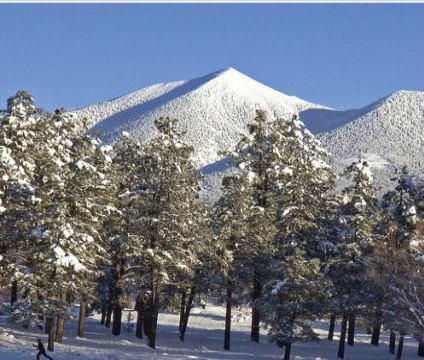


GPLET



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# GASB 77 (Tax abatement disclosures in Financial Reports – starting with FY 16-17)

Defines tax abatement as:

- Agreement between a government and a person
- Government promises to forego tax revenues
- Person promises an action that contributes to economic development or benefits the government or its citizens

Must disclose:

- Tax abatement agreements (City's plus others')
- Gross dollar amount of taxes abated (FY)

**Flagstaff implementation –**

- Reporting property tax abatement agreements (3) only, not other GPLET leases



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# City Building Leases - GPLET exemptions

## Flagstaff perspective –

- GPLET exemptions serve community needs
- City receives rent and remits local transaction privilege tax (“TPT”), if applicable

## A.R.S. § 42-6208 Exemption# & examples:

1. U.S. Geological Survey – government
2. Affordable Housing – public housing
4. Orpheum, Theatrikos - performing arts
5. Pulliam Airport – aviation
7. NAIPTA – public bus system
12. Chamber of Commerce - 501(c)(6)
13. Boys & Girls Club, NACET – 501(c)(3)
15. Tenant – residential rental



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# GPLET exempt lease



## U.S. Geological Survey

- Build to suit by City, financed by bonds
- Leased to USGS, negotiated rent to recover operating costs and debt service
- Negotiations in progress for new building (\$20 million)

At the Flagstaff Science Campus , more than 200 scientists, technicians, and support staff provide research, monitoring, and technical advancements in planetary geology and mapping, biology and ecology, Earth-based geology, hydrology, and changing climate and landscapes.

## GPLET exemption: governmental activities



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# GPLET exempt lease



## Northern Arizona Center for Emerging Technologies

- Built by City, partially financed with grants, NAU partnership
- NACET is prime lessee, manages business "incubator" and "accelerator" facilities
- Subleased to business startups and entrepreneurs, primarily for research and development, science, technology and clean energy focused businesses
- Low cost rent, limited term (6-24 months)
- Conference facilities available for public use (for a fee)

**GPLET exemption: 501(c)(3)**



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# GPLET reforms & the Gift Clause

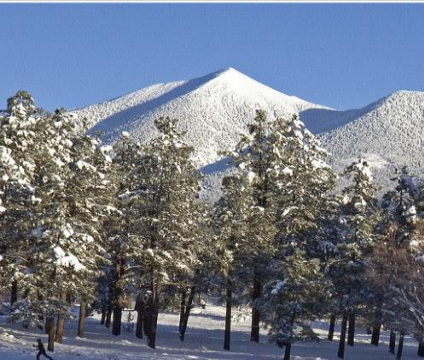
## GPLET reforms (2010, 2017)

- Higher GPLET lease rates
- Maximum 8 year GPLET tax abatement in central business district/slum blighted area, must transfer land and building to prime lessee at conclusion (restore property to tax rolls)
- City to now calculate and report GPLET (vs. lessee)



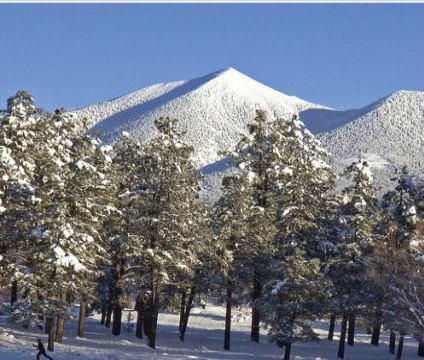
## *Turken v. Gordon* (2010)

- Community must receive a direct public benefit in exchange for any tax abatement  
(anticipated job creation and economic growth alone are not enough)



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# GPLET lease rates today

GPLET rates (A.R.S. § 42-6203.B)(rev. 9/2016):

1 story office	\$2.25/sq.ft./year
2-7 story office	\$2.59
8+ story office	\$3.49
Retail	\$2.83
Warehouse/industrial	\$1.52
Residential rental	\$0.86
All others	\$2.25
Parking	\$225.11



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# What will it cost for a new 50,000 sq.ft. warehouse in City?

## Property tax+ vs. GPLET

AD Valorem:	Full Cash Value	FCV/LPV Ratio	Limited Property Value	Assessment Ratio	Assessed Value	Tax Rate	Tax
Light Manufacturing - Class S	\$2,811,833	0.9044	\$2,543,022	18.00%	\$457,743.92	9.54	<b>\$43,668.77</b>
Light Manufacturing - Class C	\$3,023,299	0.9044	\$2,734,272	18.00%	\$492,168.89	9.54	<b>\$46,952.91</b>
Storage Warehouse - Class S	\$3,600,426	0.9044	\$3,256,225	18.00%	\$586,120.55	9.54	<b>\$55,915.90</b>
Distribution Warehouse - Class S	\$3,683,586	0.9044	\$3,331,435	18.00%	\$599,658.33	9.54	<b>\$57,207.40</b>
Storage Warehouse - Class C	\$3,967,122	0.9044	\$3,587,865	18.00%	\$645,815.72	9.54	<b>\$61,610.82</b>
Distribution Warehouse - Class C	\$4,120,864	0.9044	\$3,726,909	18.00%	\$670,843.69	9.54	<b>\$63,998.49</b>
Heavy Manufacturing - Class S	\$5,059,779	0.9044	\$4,576,064	18.00%	\$823,691.54	9.54	<b>\$78,580.17</b>
Heavy Manufacturing - Class C	\$5,330,830	0.9044	\$4,821,203	18.00%	\$867,816.48	9.54	<b>\$82,789.69</b>
<b>GPLET:</b>	<b>Square Foot</b>	<b>Rate</b>	<b>GPLET</b>				
Warehouse/Industrial Structure	50,000	\$1.52	<b>\$76,000.00</b>				

Based on 104-07-002B. Scenario based on 50,000 SF warehouse built new in 2017 on 3.21 acres of land with a rail spur, in the center of Flagstaff.

Ad Valorem valuation includes warehouse building with some interior build out, loading wells, loading docks and 70,000 sf of asphalt paving.

(+) Business owner paying property tax will also have costs of acquiring property.



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# What will it cost for a new 50,000 sq.ft. warehouse in City?

## Market lease rate vs. GPLET +

Flagstaff market lease rates:

Office space \$8 – 26/sq.ft./year (Avg. \$17)

Industrial space \$6 – 19/sq.ft./year (Avg. \$11)

Lease terms and location vary

**Market lease** = 50,000 x \$6 = \$300,000/year

50,000 x \$11 = \$550,000/year

**GPLET** = 50,000 x \$1.52 = \$76,000/year

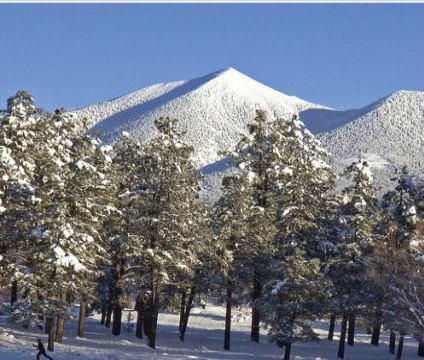
(+) Business owner paying GPLET also will have to pay City rent. City lease rates are typically established through a competitive procurement, but may be below market.



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# What are City economic development needs today, what are we doing, and how are we using GPLET laws?

- Affordable housing
  - ~ Multi-faceted housing program
  - ~ RFP for lease/sale of land (low income housing tax credit project)
  - ~ A.R.S. § 42-6208(2), (15): GPLET exemptions for public housing, residential rental to occupant
- Downtown parking structure
  - ~ Installing downtown parking meters, collecting fees to pay for project
  - ~ Possible IGA with County for shared facility
  - ~ A.R.S. § 42-6208(14): GPLET exemption for parking mgr.
- Job creation/high paying jobs
  - ~ See GPLET exemption examples (USGS, NACET)



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# Concluding remarks

## Flagstaff perspective –

- Overall, 2010 and 2017 reforms help ensure public funds are used for public benefit, and are beneficial.
- GPLET exemptions are vital to serve community needs.
- GPLET lease rates today may not make economic sense for a new business choosing a business site, when considering its options: City building lease, market lease, or property ownership.
- City sees new role in reporting GPLET payments, and property tax abatements per GASB 77 as beneficial.



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# Thank you, Arizona Department of Revenue, for inviting us to share Flagstaff's perspective!

## Thank you for your contributions to this presentation:

- Dave McIntire, Community Investment Director (928) 213-2907
- John Saltonstall, Business Expansion & Retention Manager (928) 213-2966
- Gail Jackson, Business Attraction Manager (928) 213-2965
- Sterling Solomon, City Attorney (928) 213-2043
- Anja Wendel, Sr. Assistant City Attorney (928) 213-2047 (Presenter)
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- Kelly Murphy, County Appraisal Manager (928) 679-7972



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# GPLET Overview

SEPTEMBER 1ST, 2017

# GPLET – WHAT IS IT?

- ▶ Government Property Lease Excise Tax (“Gee-Plet”)
- ▶ Authorized by State as economic development tool in 1996
  - ▶ ARS Title 42, Chapter 6, Article 5
- ▶ Government-owned property is not subject to property tax
- ▶ Provides a way to collect tax from private entities who lease government property
  - ▶ Excise Tax as substitute to Property Tax
  - ▶ Without GPLET, tax would be \$0

# GPLET – WHAT IS IT USED TO DO?

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There are two fundamental ways GPLET is used:

1. To tax non-government uses which utilize space within city, town, county and county stadium district property with an excise tax
2. As an economic redevelopment tool to facilitate revitalization

# GPLET AS A REDEVELOPMENT TOOL

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- ▶ It helps solve the financial gap for infill development challenges:
- ▶ Harder to design
- ▶ Entitlement Process
- ▶ Environmental issues
- ▶ Development costs
- ▶ Land assemblage





# THE ECONOMIC INCENTIVE\*

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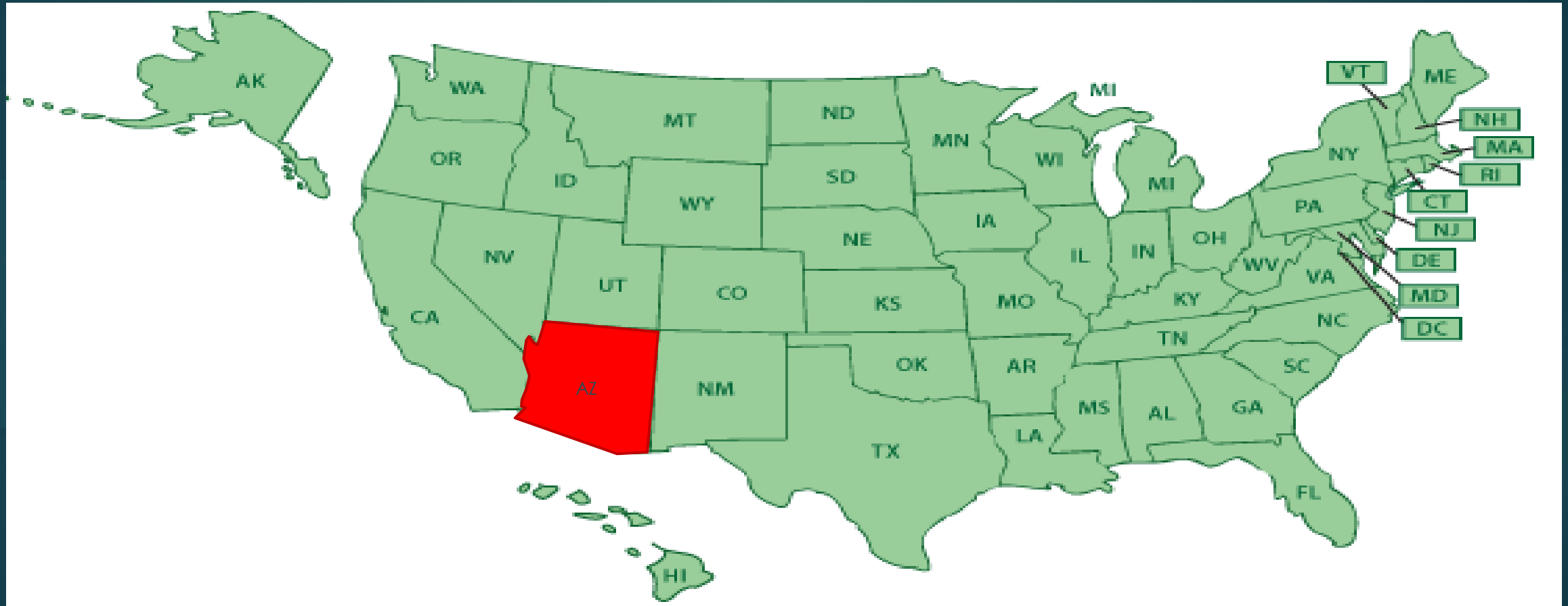
- ▶ Excise Tax is not always less than Property Tax
- ▶ Subject to Government Lessor approval
- ▶ Must provide taxing jurisdictions 60 day & 30 day notices
- ▶ Excise Tax for up to 25 Years; or
- ▶ Abatement of Excise Tax (8 year max)
  - ▶ Must be Within Both Redevelopment Area and Single CBD
  - ▶ Must Improve Value by 100%

*\*GPLET Can Be Used in Areas Outside CBD (different terms; not typical)*

# Why Not Something Else?

# TAX INCREMENT FINANCING – LEGAL IN 49 STATES

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# LEGISLATIVE CHANGE IMPACTS

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- ▶ 2009, Third Special Session (Budget Bill)
  - GPLET property value added to state funding calculation for schools
  - Shifted equalization assistance from the State to local property owners
- ▶ 2010, Regular Legislative Session (GPLET Changes)
  - Made Counties responsible for reporting & collection
  - Adjusted Excise tax rates
  - Imposed term limit of 25 years
  - Imposed notice requirements

# LEGISLATIVE CHANGE IMPACTS

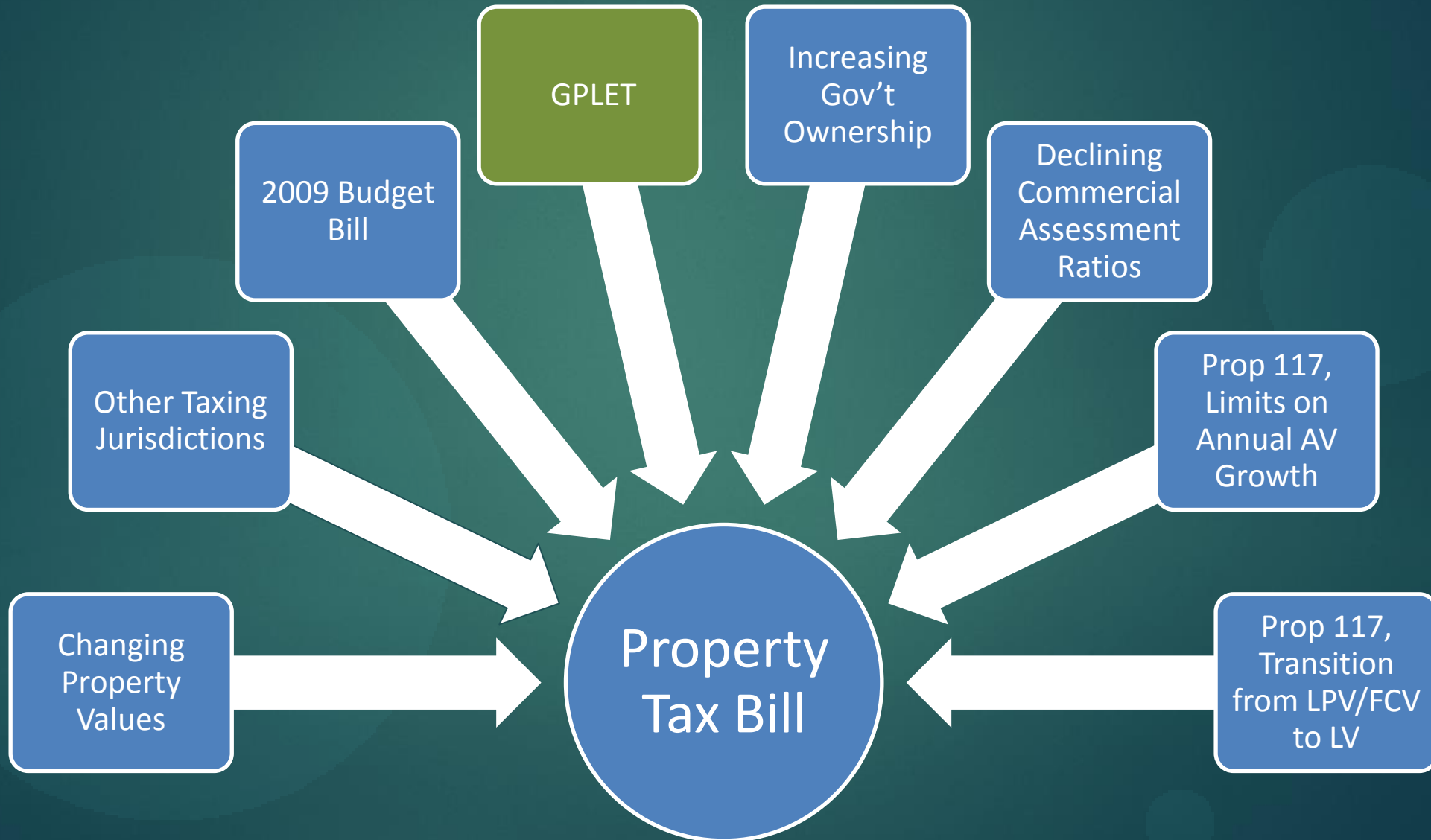
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- ▶ 2017, Regular Legislative Session
  - GPLET now only allows for an 8 year abatement of property tax OR up to 25 years of excise tax
  - Not retroactive to existing development agreements
  - Government Lessor's are responsible for calculating and reporting



# MANY FACTORS IMPACT PROPERTY TAXES

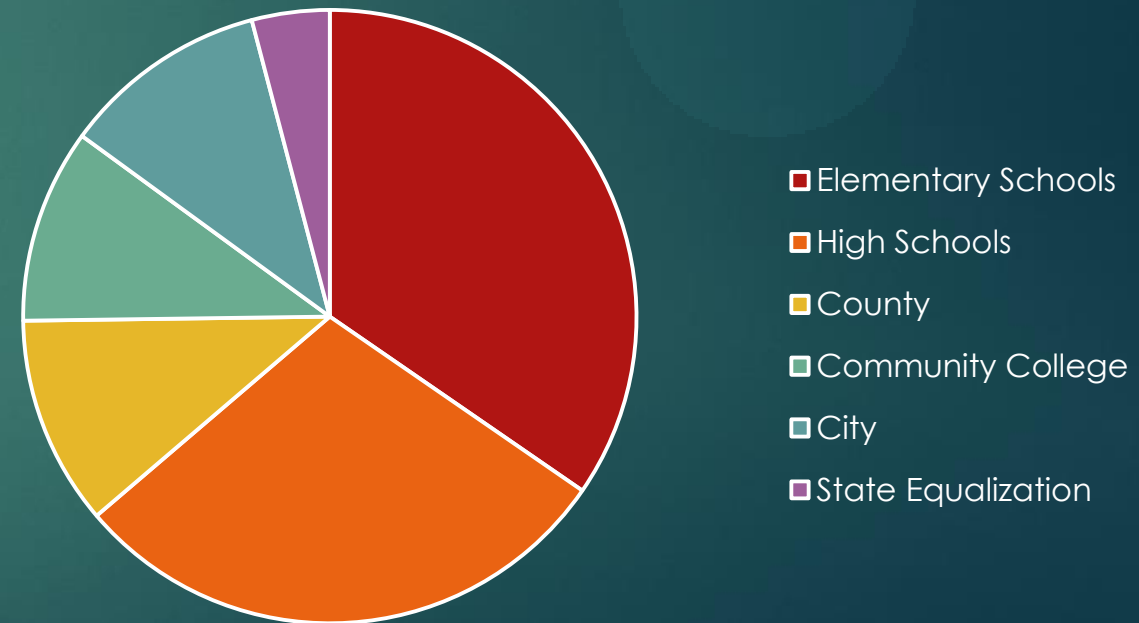
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# WHERE DOES THE PROPERTY TAX GO?

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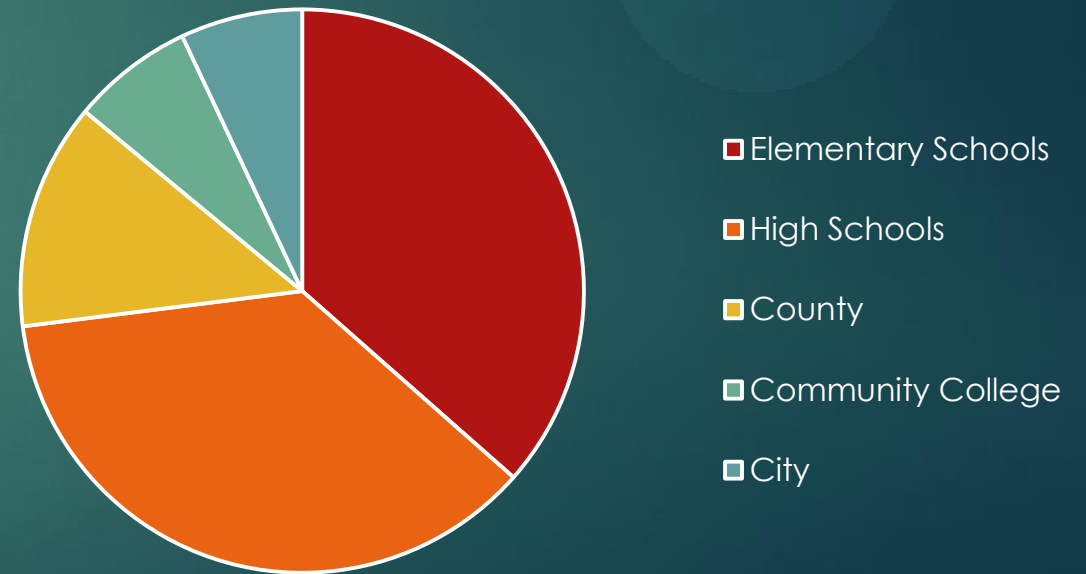
- ▶ Downtown property owners have their property taxes distributed as follows:
- 34.6% elementary school district
- 29.2% high school district
- 11% county
- 10.2% community college
- 10.9% city
- 4.1% State equalization



# WHERE DOES THE EXCISE TAX GO?

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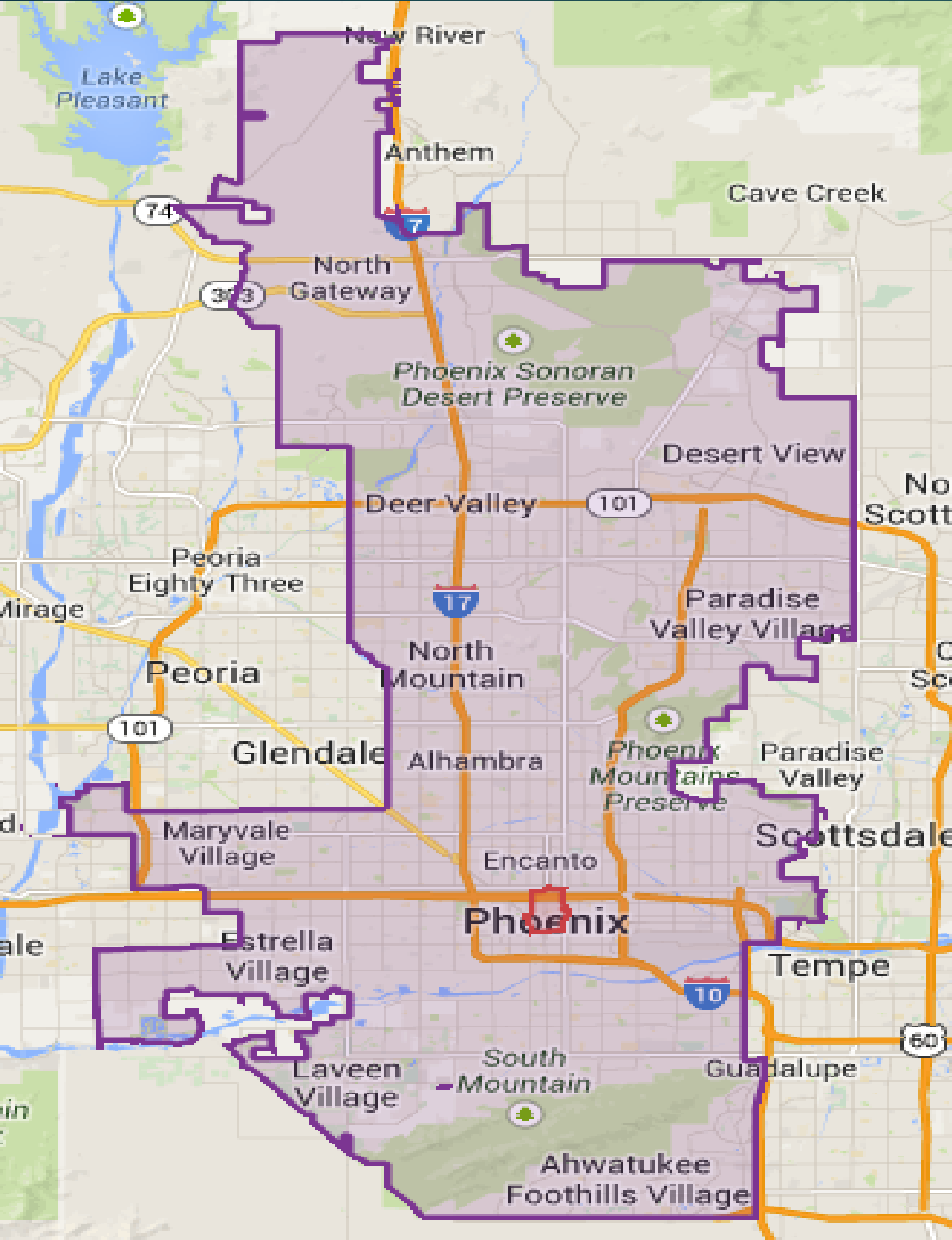
- ▶ County Treasurer collects the excise tax revenue and distributes the revenue as follows:
  - 36.5% elementary school district
  - 36.5 % high school district
  - 13% county
  - 7% community college
  - 7% city





# GPLET IN PHOENIX

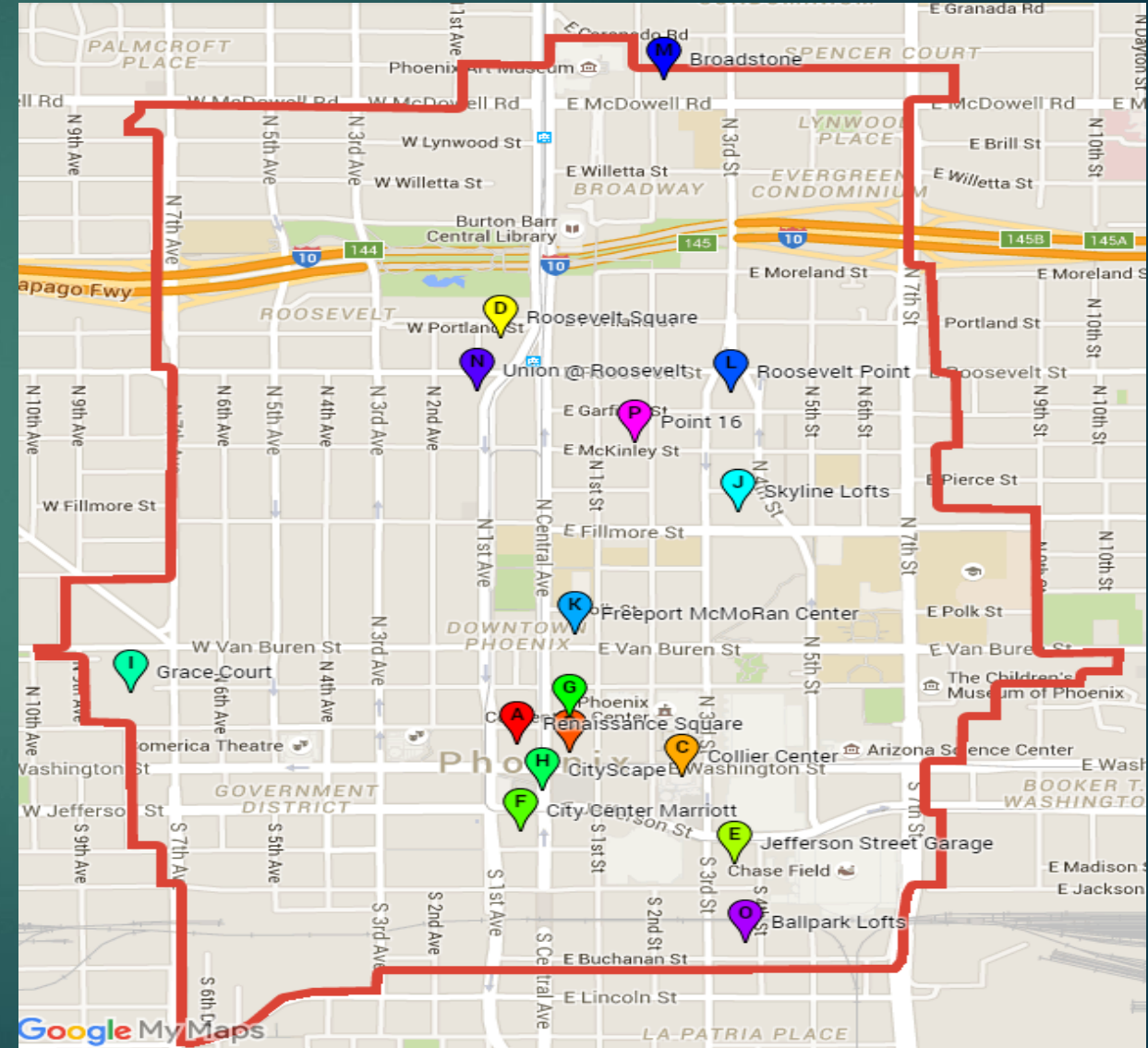
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- ▶ Used almost exclusively within the Downtown Redevelopment Area and Central Business District
  - ▶ Phoenix – 500+ sq mi
  - ▶ GPLET Area – 1.5 sq mi
- \*There are a number of non-economic development GPLETs; e.g. public housing and aviation properties

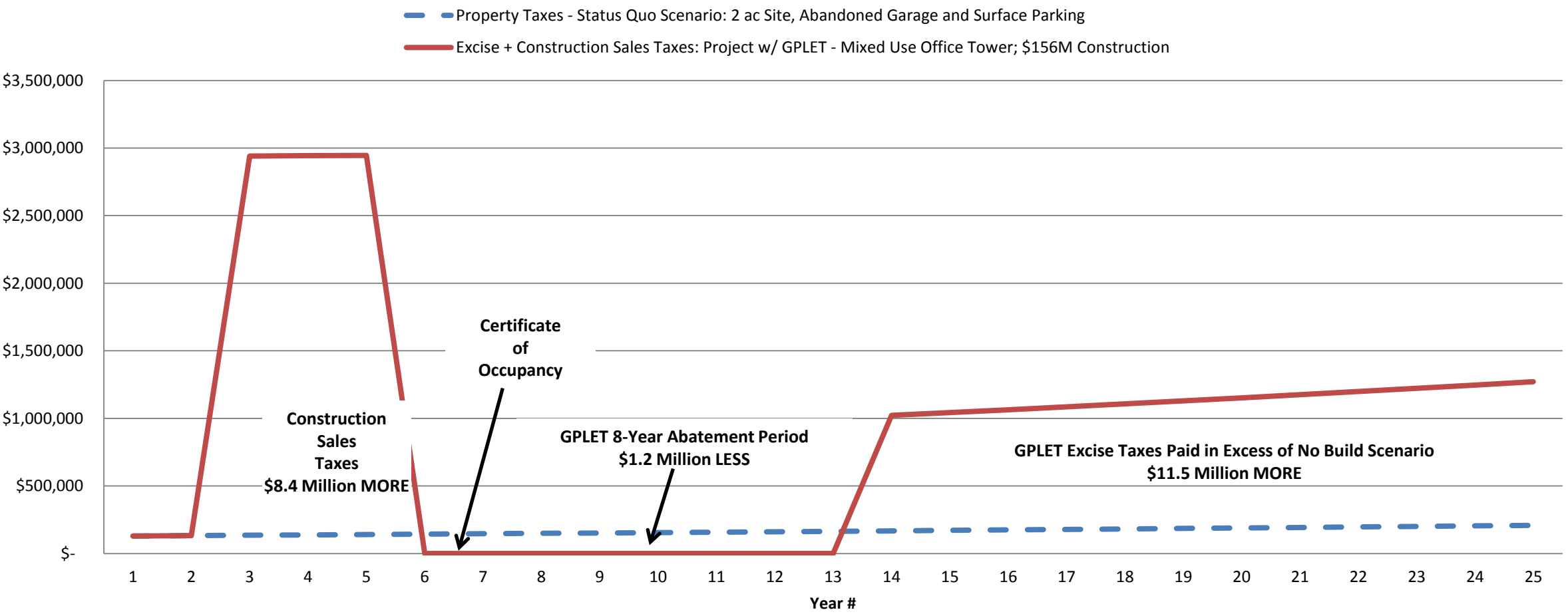
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- Note: Other Phoenix Departments also manage GPLET agreements



# EXAMPLE: OFFICE TOWER TAX COMPARISON

Annual Taxes Generated - Status Quo vs. Project w/ GPLET





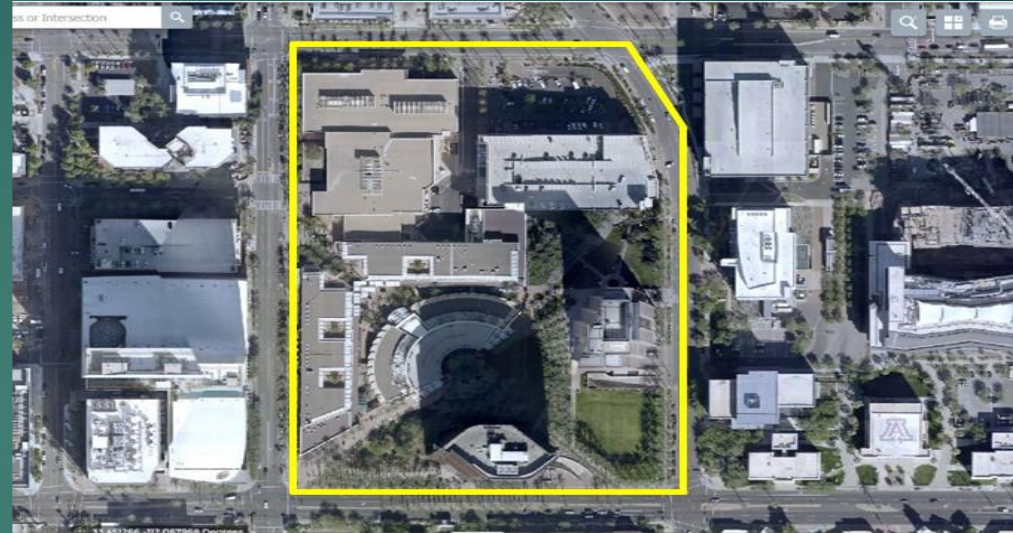
# GPLET SUCCESSES

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Arizona Center -1982



Arizona Center - 2016



Arizona Center ended GPLET in 2011

Camden - 1997



Camden - 2016



Camden ended GPLET in 2012

# REDEVELOPMENT IMPACTS OF GPLET

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- Without GPLET, projects would not have been built
- Results:
  - Billions in capital investment
  - More downtown jobs (construction & permanent)
  - More downtown residences, restaurants & shops
  - Enhanced downtown property values





# Questions